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11 Easterday

HONORABLE WHITMAN L. HOLT

Hearing Date: December 21, 2021
Hearing Time: 11:00 a.m.
Location: Telephonic
Telephone Number: 877-402-9757
Telephonic Access Code: 7036041

9 UNITED STATES BANKRUPTCY COURT
10 EASTERN DISTRICT OF WASHINGTON

11 In re
12 EASTERDAY RANCHES, INC., *et al.*
13 Debtors¹.

15 EASTERDAY RANCHES, INC. and
16 EASTERDAY FARMS,
17 Plaintiffs,
18 v.
19 ESTATE OF GALE A. EASTERDAY
20 (DECEASED), KAREN L. EASTERDAY,
21 CODY A. EASTERDAY, and DEBBY
22 EASTERDAY,
23 Defendants.

Chapter 11

Lead Case No. 21-00141-WLH
Jointly Administered

Adv. Pro No. 21-80050 (WLH)

**NOTICE AND MOTION TO
DISQUALIFY PACHULSKI
STANG ZIEHL & JONES LLP
AND BUSH KORNFELD LLP
AS COUNSEL FOR DEBTORS**

26 ¹ This case is jointly administered with *In re Easterday Farms*, Case No. 21-00176-WLH11.

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LLP AND BUSH KORNFELD LLP AS COUNSEL FOR DEBTORS - 1

1 ESTATE OF GALE A. EASTERDAY
2 (DECEASED), KAREN L. EASTERDAY,
3 CODY A. EASTERDAY, and DEBBY
4 EASTERDAY,

5 Counterclaim Plaintiffs,

6 v.

7 EASTERDAY RANCHES, INC.,
8 EASTERDAY FARMS,

9 Counterclaim Defendants.

10 INTRODUCTION

11 Karen Easterday, individually and as the representative of the estate of
12 Gale A. Easterday, moves, pursuant to 11 U.S.C. §§ 101(14), 105(a), and 327(a)
13 and (c) for Pachulski Stang Ziehl & Jones LLP (“PSZJ”) and Bush Kornfeld LLP
14 (“BK”) to be disqualified as counsel for Easterday Ranches, Inc. and Easterday
15 Farms (together, “Debtors”) in the above-captioned adversary proceeding (the
16 “Adversary Proceeding”). Mrs. Easterday previously raised this issue in court, but
17 since PSZJ and BK have continued representing both Debtors in this Adversary
18 Proceeding [adv. pro. doc. nos. 26 and 27], a formal motion is required.

19 BACKGROUND

20 Pachulski Stang Ziehl & Jones and Bush Kornfeld’s Employment

21 Easterday Ranches, Inc. filed for bankruptcy protection on February 1, 2021
22 (“Ranches”). Easterday Farms filed for bankruptcy protection on February 8, 2021
23 (“Farms”). Ranches and Farms’ bankruptcy cases are being jointly administered,
24 but are separate estates and have not been substantively consolidated. The two
25 Debtors do not have a unity of creditors nor a unity of assets.

26 PSZJ and BK were employed as counsel for Debtors in the main bankruptcy
case and, in turn, in this Adversary Proceeding, pursuant to court orders (the

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1 “Employment Orders”). [Main Case Doc. Nos. 386 and 385.] Prior to entry of the
2 Employment Orders, the Office of the United States Trustee (“UST”) objected to
3 PSZJ and BK’s employment applications because of concerns related to conflicts
4 between the two estates (the “Objections”). [Main Case Doc. Nos. 313 and 312.]

5 In replying to the UST’s Objections, PSZJ and BK stated: “If an actual
6 conflict of interest between the Debtors arises, the estates already have entities
7 capable of addressing the issue: the two creditors’ committees.” [Main Case Doc.
8 No. 338, p. 4, line 3.] The Ranches and Farms committees responded to the
9 Objections as well. The Ranches Committee stated: “And, to the extent that
10 Ranches fails to pursue any cause of action for the benefit of its estate, the Ranches
11 Committee believes that it is positioned to prosecute or defend such action(s),
12 including any claim(s) against Farms. * * * In this manner, issues of conflict of
13 interest may be addressed.” [Main Case Doc. No. 339, p. 3, lines 10-16.] The
14 Farms Committee stated: “[T]he Farms Committee understands the U.S. Trustee’s
15 concerns and takes them very seriously.” [Main Case Doc. No. 340, p. 2,
16 lines 9-10.] If “debtors eventually become adverse to each other, the conflicted
17 professionals would need to withdraw from those disputes.” *Id.* at p. 3,
18 lines 12-13.

19 On March 15, 2021, the court held a hearing to consider the PSZJ and BK
20 employment applications and the Objections thereto. During that hearing, counsel
21 for PSZJ stated that allocation between Debtors’ estates as to property proceeds
22 “will absolutely have to happen in this case.” [Main Case Doc. No. 372.] The
23 court ultimately overruled the Objections but stated that if there is a direct, live
24 adversity or if intercompany claims need to be actively pursued, the Farms
25 Committee and Ranch Committee can be deputized to do this (instead of retaining
26 conflicts counsel). *Id.* The court further stated its expectation that if there is a

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1 dispute or claim that the Farms Committee and Ranches Committee is pursuing
2 against the other, PSZJ and BK will not represent either of the Debtors but, instead,
3 act as the “honest broker” and help negotiate as between the committees. *Id.*

4 As the Complaint and Answer and Counterclaims in the Adversary
5 Proceeding make clear, a direct, live adversity has arisen. **There is an actual**
6 **conflict between Farms and Ranches because the court must determine which**
7 **of them (along with the Easterday family) owned the Sale Properties and how**
8 **much value each of the estates (along with the Easterday family) will receive**
9 **from the proceeds of the Sale. Yet PSZJ and BK continue to represent both**
10 **Debtors in the Adversary Proceeding. [Adv. Pro. Doc. Nos. 26 and 27.] PSZJ**
11 **and BK should be disqualified from doing so.**

12 *The Pending Adversary Proceeding*

13 As the court is well aware, significant real property, along with
14 improvements thereon and water rights appurtenant thereto (the “Sale Properties”),
15 were sold on or about July 30, 2021 to Farmland Reserve (the “Sale”). To
16 maximize the value of the Sale Properties, the Easterday family agreed that
17 property personally owned by them could be sold along with Debtors’ property,
18 with the understanding that the net sale proceeds would later be allocated among
19 each of Ranches, Farms, and the Easterday family. This understanding was
20 memorialized in a Cooperation Agreement prior to the Sale, which was approved
21 by the court. [Main Case Doc. No. 640.] The Cooperation Agreement expressly
22 recognized that the Easterday family personally owned portions of Cox Farm and
23 River Farm, and all of Goose Gap Farm. Pursuant to the Cooperation Agreement,
24 each of the Debtors and the Easterday Family were to stipulate to the allocation of
25 the net proceeds from the Sale or, to the extent there was a dispute about the
26 allocation of the net proceeds from the Sale, negotiate in good faith and attempt to

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1 reach agreement on a timely basis on a protocol for resolving such disputes. *Id.* at
2 sections 3 and 4.

3 Notwithstanding the terms of the Cooperation Agreement, the parties have
4 not stipulated to allocation of the net proceeds and not yet negotiated in good faith
5 to reach agreement on a protocol for resolving disputes concerning the allocation
6 of proceeds from the Sale. Instead, Debtors filed an adversary complaint against
7 Mrs. Easterday (and other family members) seeking a determination that Debtors
8 owned all of the Sale Properties and are entitled to all of the net sale proceeds (the
9 “Complaint”). [Adv. Pro. Doc. No. 1.] As set out in Mrs. Easterday’s answer and
10 counterclaims to the Complaint (“Answer and Counterclaims”), Mrs. Easterday
11 disputes this and seeks a determination by the court as to who among each of
12 Ranches, Farms, and the Easterday family owned the Sale Properties, and a
13 determination of how much of the Sale proceeds are attributed to the real property,
14 to the water rights appurtenant thereto, and to the irrigation improvements thereon.
15 [Adv. Pro. Doc. No. 14.] The Adversary Proceeding directly places in dispute the
16 competing claims and interests to the real property, water rights, and property
17 improvements—and the values of each—as between Farms and Ranches, as well
18 as the Easterday individuals. PSZJ and BK have a direct conflict of interest in
19 advocating for the interests of Ranches and Farms against one another.

20 ARGUMENT

21 There is a live and direct dispute among Ranches, Farms, and the Easterday
22 family as to who owned the Sale Properties and who should receive the net
23 proceeds of the Sale. Notwithstanding this dispute—and notwithstanding the fact
24 that the court, Debtors, and Committees acknowledged at the March 15, 2021
25 hearing that if such a dispute were to arise, PSZJ and BK could not act as counsel
26

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1 for both Debtors—PSZJ and BK continue to represent both Ranches and Farms in
2 the Adversary Proceeding. They may not.

3 In order to be employed by a debtor-in-possession, a professional must “not
4 hold or represent an interest adverse to the estate” and must be “disinterested.”
5 11 U.S.C. § 327(a).

6 To “hold an interest adverse to the estate” means (1) to
7 possess or assert any economic interest that would tend to
8 lessen the value of the bankruptcy estate or that would
9 create either an actual or potential dispute in which the
10 estate is a rival claimant; or (2) to possess a
predisposition under circumstances that render such a
bias against the estate.

11 *In re Tevis*, 347 B.R. 679, 688 (9th Cir. BAP 2006); *see also In re Farrington*,
12 No. 07–32420–elp7, 2007 WL 4365753, at *3 (Bankr. D. Or.); *In re Roberts*, 46
13 B.R. 815, 827 (Bankr. Utah 1985) *aff’d in part and rev’d in part on other grounds*,
14 75 B.R. 403 (D. Utah 1987).

15 To “represent an interest adverse to the estate” means “to serve as an
16 attorney for an entity holding such an adverse interest.” *In re Tevis*, 347 B.R.
17 at 688.

18 A person is “disinterested” if, in part, the person “does not have an interest
19 materially adverse to the interest of the estate or any class of creditors or equity
20 security holders, by reason of any direct or indirect relationship to, connection
21 with, or interest in, the debtor, or for any other reason. 11 U.S.C. § 101(14)(C).

22 The “adverse interest” and “disinterestedness” tests overlap, and include “a
23 prohibition on representing conflicting interests.” *In re Tevis*, 347 B.R. at 687.
24 These tests serve the important policy of ensuring that all professionals appointed
25 under section 327 tender undivided loyalty and provide untainted advice and
26 assistance in furtherance of their fiduciary responsibilities. *Id.*

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1 Moreover, pursuant to 11 U.S.C. § 327(c), although professionals “are not
2 disqualified ‘solely’ because of employment by or representation of a creditor, **the**
3 **bankruptcy court ‘shall’ disapprove their employment upon objection if there**
4 **is an ‘actual conflict of interest.’”** *In re Hammer*, Nos. WW–06–1373–MoDJ,
5 04–22244–SJS, 2007 WL 7540944, at *5 (9th Cir. BAP Oct. 11, 2007) (emphasis
6 added).

7 “In differentiating subsections (a) and (c) of Section 327, the courts
8 sometimes distinguish so-called ‘potential’ conflicts from the ‘actual conflicts’
9 mentioned in the statute[.]” *Id.* As the *Hammer* court explained:

10 Section 327(a), as well as § 327(c), imposes a *per se*
11 *disqualification* as trustee's counsel of any attorney who
12 has an *actual* conflict of interest [whereas] the
13 [bankruptcy] court may within its discretion—pursuant to
14 § 327(a) and consistent with § 327(c)—disqualify an
attorney who has a *potential* conflict of interest * * *.

15 *Id.* quoting *Dye v. Brown (In re AFI Holding, Inc.)*, 355 B.R. 139, 154 (9th Cir.
16 BAP 2006) (quoting *In re Marvel Entm't Group*, 140 F.3d 463, 476 (3d Cir. 1998)
17 (italics and brackets in original).

18 Here, there is an actual conflict of interest with no work-around for PSZJ
19 and BK. This is because the Bankruptcy Code does not permit a debtor-in-
20 possession to negate a conflict by signing a waiver “because the ultimate party at
21 interest is the creditors of the bankruptcy estate.” *In re Perry*, 194 B.R. 875, 880
22 (E.D. Cal. 1996). Moreover, PSZJ and BK’s dual representation in the Adversary
23 Proceeding is a conflict that may not be waived under the Washington Rules of
24 Professional Conduct (“WRPC”). WRPC 1.7(b) only permits an attorney to
25 represent a client despite a current conflict of interest where that attorney is not
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1 asserting a claim against another client in the same litigation. This, however, is
2 squarely what PSZJ and BK must do in the Adversary Proceeding.

3 The Sale Proceeds represent a limited set of funds with competing demands
4 as to ownership and valuation by Ranches and by Farms. Each Debtor entity must
5 advocate to recover as much as it can from the Sale proceeds, which proceeds **are**
6 **not enough to pay all creditors in both estates in full.** The interests of each
7 estate are not parallel, but are in direct conflict. *In re BH & P Inc.*, 949 F.2d 1300,
8 1314 (3d Cir. 1991) (considering whether estates' interests are parallel or
9 conflicting as one factor when determining whether same counsel may represent
10 multiple debtors and stating that even where a per se rule does not apply against
11 multi-debtor representation, an actual conflict in interest will disqualify the
12 attorney). Where counsel's professional judgment and advocacy would be clouded
13 by divided loyalty, as it is here, such counsel must be disqualified. *In re*
14 *WM Distribution, Inc.*, 571 B.R. 866, 874 (Bankr. D. NM 2017) ("A court should
15 approve a debtor's choice of counsel, 'only when that professional's judgment and
16 advocacy would be unclouded by divided loyalty.'") (quoting *In re Interwest*
17 *Business Equipment, Inc.*, 23 F.3d 311, 316 (10th Cir. 1994)); *see also Rome v.*
18 *Braunstein*, 19 F.3d 54, 58 (1st Cir. 1994) (§ 327's requirements "serve the
19 important policy of ensuring that all professionals appointed pursuant to
20 section 327(a) tender undivided loyalty and provide untainted advice and
21 assistance in furtherance of their fiduciary responsibilities.").

22 Anticipating that a potential conflict could become an actual conflict – like
23 now exists in the Adversary Proceeding—the court stated at the March 15th
24 hearing that in such a circumstance, PSZJ and BK would not act as counsel for
25 either Debtor. But that has not occurred here notwithstanding the fact that counsel
26 for Mrs. Easterday has raised this conflict concern multiple times.

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1 As the court in *In re Raymond Professional Group, Inc.* cautioned,

2 [a]n attorney who is allowed to represent multiple
3 debtors in * * * Chapter 11 cases must be especially
4 careful not to violate these ongoing employment
5 requirements by preferring one debtor over another.
6 'Each debtor-in-possession owes a fiduciary duty to its
7 creditors. * * * Thus, when an attorney representing
8 multiple debtors-in-possession works to benefit one
9 debtor's estate or creditors at the expense of another
10 debtor's estate or creditors, the attorney risks breaching
its fiduciary duties to the forsaken debtor-in-possession.
In such a situation, the attorney would represent an
interest—that of the preferred debtor-in-possession—
adverse to the forsaken debtor-in-possession and its
creditors, a disqualifying conflict.

11 421 B.R. 891, 903 (Bankr. N.D. Ill. 2009).

12 That is precisely what is occurring in this case. PSZJ and BK cannot satisfy
13 their fiduciary obligations to **both** Debtors while simultaneously responding to
14 discovery and preparing for trial on questions of which **particular** Debtor owned
15 certain property and how much that property is worth such that **that particular**
16 **Debtor's estate** would benefit from any recovery at the expense of the other
17 Debtor's estate.

18 Rather, the concurrent representation of Ranches and Farms in the
19 Adversary Proceeding by PSZJ and BK means that the Debtors' estates are
20 competing with one another for the same funds and using the same lawyers to do
21 so. This runs afoul of the requirements of section 327 and means that PSZJ and
22 BK are not disinterested and represent interests adverse to each estate. To continue
23 such representation is a direct breach of ethics under the Washington Rules of
24 Professional Conduct. *MidTown Limited Partnership v. Bangasser*, 13
25 Wash.App.2d 1046 (2020) ("RPC 1.7 prohibits a lawyer from representing a client
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1 if a concurrent conflict of interest exists. ‘A concurrent conflict of interest exists
2 if: (1) the representation of one client will be directly adverse to another client; or
3 (2) there is a significant risk that the representation of one or more clients will be
4 materially limited by the lawyer's responsibilities to another client * * *.’”)
5 (internal citations omitted); *In re Marriage of Wixom and Wixom*, 182 Wash.App.
6 881 (2014) (disqualifying attorney and stating that lawyer represented conflicting
7 interests when, on behalf of one client, it was the lawyer's duty to contend that
8 which the lawyer's duty to another client required him to oppose).

9 The issue of who can be appointed as new counsel on behalf of Ranches and
10 Farms also needs to be revisited. It is not as simple as appointing the creditors
11 committees as counsel for the respective Debtors. The Adversary Proceeding is
12 not a dispute over intercompany accounts, as was discussed at the employment
13 hearing. Rather, the result of the Adversary Proceeding may be that the Farms’
14 estate is solvent and has significant equity for the partners. The counsel
15 representing the Farms’ estate has a fiduciary duty to represent all creditors,
16 including equity, and must advocate for that position. *In re Asarco, L.L.C.*, 650
17 F.3d 593, 601 (5th Cir. 2011) (recognizing debtor-in-possession has fiduciary
18 duties to debtor, creditors, and equity holders); *In re Nucletron Manufacturing*
19 *Corp.*, No. 93-34486S, 1994 WL 16191611, at *3 (Bankr. E.D. Va. March 17,
20 1994) (“The debtor-in-possession owes not only a fiduciary duty to the creditors
21 but to the equity holders as well.”) citing *Commodity Futures Trading Commission*
22 *v. Weintraub*, 471 U.S. 343 (1985).

23 As currently constituted, the Farms’ committee counsel only represents the
24 interests of the Farms’ general unsecured creditors. It does not represent the
25 interests of the entire bankruptcy estate, which a debtor’s counsel would be
26 charged with representing. Thus, either conflicts counsel needs to be appointed for

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1 the purposes of the Adversary Proceeding or this Court needs to expressly expand
2 the committees counsels' duties in the Adversary Proceeding to include
3 representation of the entire estate, not just the interests of the unsecured creditors.
4 Otherwise, the committees' representation would stop at payment of its present
5 constituents' claims and leave the remainder of Debtors' estates without proper
6 representation.²

7 CONCLUSION

8 Legal ethics, as well as the employment requirements imposed on
9 bankruptcy estate professionals, ensure transparency and unbiased representation
10 of, and undivided loyalty to, the bankruptcy estate, its creditors, and equity holders.
11 Pachulski Stang Ziehl & Jones LLP and Bush Kornfeld LLP must be disqualified
12 as counsel for Debtors in the Adversary Proceeding because they are not
13 disinterested and hold interests adverse to each estate. They simply cannot
14 advocate for both estates in the Adversary Proceeding. Consistent with the
15 comments of PSZJ, the Ranches Committee, the Farms Committee, and the court
16 leading up to and at the March 15, 2021 hearing, and for the reasons set forth
17 herein, this court must order PSZJ and BK to immediately cease representing

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25 ² The Easterdays cannot represent the equity interests as they will be representing
26 their own individual ownership interests and are not being compensated by the
bankruptcy estate to represent the estate's interests.

1 Ranches and Farms in this Adversary Proceeding. Appropriate counsel that can
2 fully represent the interests of each respective debtor must be appointed to replace
3 PSZJ and BK.

4 Dated: December 14, 2021.

5 TONKON TORP LLP

6
7 By /s/ Timothy J. Conway

8 Timothy J. Conway, WSBA 52204
9 Attorneys for Karen L. Easterday,
10 individually and as personal
representative of the Estate of Gale A.
Easterday

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